

## Attachment 2 to Staff Report

### PUBLIC PURPOSES AND BENEFITS OF SETTLEMENT AGREEMENT

#### **1. Overview of Settlement Agreement**

The Office of the Mayor has recommended that the San Diego City Council (Council) approve a proposed Settlement Agreement and Mutual Release (Settlement Agreement) negotiated during confidential mediation discussions by and among the following parties (collectively, Settling Parties): (a) the City of San Diego (City); (b) Cisterra Partners, LLC, a California limited liability company, and two of its affiliated business entities, CCP 1200, LLC, a Delaware limited liability company, and 101 Ash, LLC, a Delaware limited liability company (collectively, Cisterra); and (c) Wilmington Trust, National Association, (i) as trustee of CGA Capital Credit Lease-Backed Pass-Through Trust, Series 2015 CTL-1, and (ii) as trustee of CGA Capital Credit Lease-Backed Pass-Through Trust, Series 2017 CTL-1 (collectively, Lender). The Settlement Agreement is included as Attachment 1 to the City staff report to the Council (Staff Report), and all capitalized terms in this Attachment 2 have the same meaning ascribed to them in the Settlement Agreement unless otherwise specified. The Office of the Mayor offers the information and analysis in this Attachment 2 to the Council as a means to both explain the key financial considerations for the City in the Settlement Agreement and describe the public purposes and benefits to the City of the Settlement Agreement.

Through the Settlement Agreement, the Settling Parties will agree to the following key terms: (a) the Settling Parties will dismiss with prejudice the claims between them in pending litigation involving the Civic Center Plaza property located at 1200 Third Avenue and 201 A Street in downtown San Diego (CCP Property) and the 101 Ash Street property in downtown San Diego (101 Ash Property); (b) the Settling Parties will release known and unknown claims against each other with respect to the CCP Property and the 101 Ash Property (collectively, Properties); (c) Cisterra and the City will terminate the existing 20-year lease-to-own agreements for the Properties, defined in Recitals B and D of the Settlement Agreement, respectively, as the CCP Lease (dated March 13, 2015) and the 101 Ash Lease (dated January 3, 2017); (d) the City will acquire fee title ownership of the CCP Property for a purchase price \$46,071,829.19, assuming the acquisition occurs on the target closing date of July 11, 2022 (CCP Purchase Price); (e) the City will acquire fee title ownership of the 101 Ash Property for a purchase price of \$85,719,062.23, assuming the acquisition occurs on the target closing date of July 11, 2022 (101 Ash Purchase Price); (f) all financing documents associated with the loans issued by Lender to Cisterra for Cisterra's earlier acquisition of the CCP Property and the 101 Ash Property, defined in Recitals B and D of the Settlement Agreement as the CCP Financing Documents and the 101 Ash Financing Documents, respectively, will be terminated and of no further force or effect; (g) Lender will waive any yield maintenance fees, prepayment penalties, or similar fees or penalties for prepayment of the loans evidenced and secured by the CCP Financing Documents and the 101 Ash Financing Documents; (h) Cisterra will pay the aggregate total of \$7,452,500 (which represents 100 percent of Cisterra's profit on the 101 Ash Lease transaction) for the City's benefit during Fiscal Year 2023 in two separate installments, with \$2,626,250 due upon the closing of the City's acquisition of the Properties (Closing) and the remaining \$4,826,250

due on or before June 30, 2023; (i) the City will have no obligation to pay any portion of fees and costs incurred by Cisterra or Lender in the mediation of the Dispute or the negotiation of the Settlement Agreement; and (j) the City will indemnify Cisterra and Lender for certain pending and future claims related to the Properties, the 101 Ash Renovations, and pending and future litigation, as further specified in Section 11 of the Agreement.

The Settling Parties' dismissal with prejudice of the claims between them will include their respective claims in the following lawsuits: (a) the 101 Ash Lawsuit and the CCP Lawsuit (i.e., the pending lawsuits in which the City has alleged the CCP Lease and the 101 Ash Lease are void under California Government Code section 1090 due to the undisclosed financial conflict of interest of the City's prior "volunteer" real estate consultant, Jason Hughes); (b) the CCP Unlawful Detainer Action (i.e., the pending, but inactive lawsuit in which Lender's affiliate has sought to evict the City from the Civic Center Plaza building for prior nonpayment of rent under the CCP Lease); and (c) the Bahena Lawsuit, the Perez Lawsuit, and the Guerrero Lawsuit (i.e., the pending lawsuits in which Cisterra has filed cross-complaints against the City for declaratory relief and indemnity in connection with the alleged exposure of various plaintiffs to asbestos-containing materials at the 101 Ash Property). The Settlement Agreement will not result in the dismissal or resolution of claims that the City has or may have against various other persons or entities, including, but not limited to, Jason Hughes, Hughes Marino, Inc., a California corporation, the carriers of any insurance policies applicable to the 101 Ash Property, or any contractors involved in the 101 Ash Renovations (i.e., the renovations and reconfigurations in the office building at the 101 Ash Property that occurred after signature of the 101 Ash Lease).

The estimated purchase price for each of the Properties, defined in Sections 2.8 and 2.10 of the Settlement Agreement as the CCP Purchase Price and the 101 Ash Purchase Price, respectively, is based on a calculation as of July 11, 2022, which is the target date of the Closing under the Settlement Agreement, although the Parties may conduct the Closing at a later date. The Closing will occur no earlier than July 11, 2022, and if the Closing occurs after that date, the final amount of the CCP Purchase Price will be adjusted to reflect a daily increase of \$4,350.57 for the CCP Property, and the final amount of the 101 Ash Purchase Price will be adjusted to reflect a daily increase of \$7,050.43 for the 101 Ash Property.

## **2. Valuation of, and Purchase Price for, Civic Center Plaza Property**

The City obtained a restricted appraisal for the CCP Property with an effective date of December 31, 2021, included as Attachment X to the Staff Report (CCP Appraisal). Based on the CCP Appraisal, the CCP Property has a land value of \$10-15 million in a vacant condition and a total value of \$87 million if the existing improvements are renovated and leased to stabilized occupancy. The CCP Appraisal ultimately concluded that the CCP Property has a total value of \$26.0-41.6 million after factoring in the estimated renovation and lease-up costs.

The CCP Purchase Price is approximately \$46.1 million, which is based on the outstanding amount of the CCP Loan, plus nominal late fees and penalties associated with the City's delayed payment of rent under the CCP Lease for two months until the Parties reached a temporary "standstill" agreement in the CCP Unlawful Detainer Action. The CCP Purchase Price is less

than the upper range of the appraised value of the CCP Property assuming renovated and leased-up building improvements, but greater than the total appraised value of the CCP Property after factoring in the estimated renovation and lease-up costs.

From a strictly financial standpoint and putting aside the public purposes and benefits of the Settlement Agreement described in Part 4 below, the Office of the Mayor believes the City's payment of approximately \$46.1 million for the CCP Property is reasonable and justified because: (a) the City will reserve its right to recover, in continuing litigation against Jason Hughes, the entirety of Hughes' profits of approximately \$5 million from the Prior CCP Transactions due to his undisclosed financial conflict of interest; and (b) the figure of \$46.1 million is derived from the original CCP Loan amount, which included Cisterra's profits of approximately \$6.2 million from the Prior CCP Transactions – an amount that the City may or may not recover if the City decides not to settle with Cisterra and to continue litigating its claims against Cisterra. If the City ultimately recovers Hughes' profits from the Prior CCP Transactions (a result that seems very likely, though not guaranteed), the CCP Purchase Price can be viewed as a net cost of approximately \$41.1 million to the City, which is less than the upper range of property value reflected in the CCP Appraisal.

### **3. Valuation of, and Purchase Price for, 101 Ash Street Property**

The City obtained a restricted appraisal for the 101 Ash Property with an effective date of December 31, 2021, included as Attachment W to the Staff Report (101 Ash Appraisal). Based on the 101 Ash Appraisal, the 101 Ash Property has a land value of \$36-42 million in a vacant condition. The 101 Ash Appraisal examines two different valuation scenarios for future use of the 101 Ash Property, identified as Options 1 and 2. Under Option 1, the existing building would be demolished to create a vacant site available for redevelopment. The value of the 101 Ash Property under Option 1 is \$4.08-10.08 million, after deducting estimated costs for building demolition and asbestos abatement. Under Option 2, asbestos removal and interior renovations would be completed to place the building in an occupiable condition. Given the appraiser's high estimate for remediation and renovation costs, the 101 Ash Property has a negative value under Option 2, rendering this option infeasible in the appraiser's estimation.

The 101 Ash Purchase Price is approximately \$85.7 million, which is based on the outstanding amount of the 101 Ash Loan, plus late fees and penalties associated with the City's nonpayment of rent since September 2020 in light of the City's contention in the 101 Ash Lawsuit that the 101 Ash Lease is void and the City's inability to occupy the office building at the 101 Ash Property. The 101 Ash Purchase Price is greater than the total appraised value of the 101 Ash Property under Options 1 and 2 in the 101 Ash Appraisal.

From a strictly financial standpoint and putting aside the public purposes and benefits of the Settlement Agreement described in Part 4 below, the Office of the Mayor believes the City's payment of approximately \$85.7 million for the 101 Ash Property is reasonable and justified because: (a) the City will reserve its right to recover, in continuing litigation against Jason Hughes, the entirety of Hughes' profits of approximately \$4.4 million from the Prior 101 Ash Transactions due to his undisclosed financial conflict of interest; (b) the City will recover 100

percent of Cisterra's profits of approximately \$7.45 million from the Prior 101 Ash Transactions; (c) the 101 Ash Purchase Price includes approximately \$12.3 million in unpaid rent under the 101 Ash Lease – an amount that the City would be required to pay in full if the City decides not to settle and is ultimately unsuccessful in its legal claims against Cisterra and Lender; (d) the substantial value deductions in the 101 Ash Appraisal are largely attributable to the estimated costs of remediating asbestos contamination and repairing or replacing mechanical systems – costs that, due to the prior 101 Ash Renovations, the City might be required to absorb even if the City prevails in its primary legal claims against Cisterra and Lender; and (e) the City will reserve the right to pursue cost recovery for asbestos removal and other remedial activities under applicable insurance policies and against the contractors who performed the 101 Ash Renovations. Given that the City will recoup Cisterra's profits from the Prior 101 Ash Transactions, and assuming the City ultimately recovers Hughes' profits from the Prior 101 Ash Transactions (a result that seems very likely, though not guaranteed) and recovers unknown amounts from insurance carriers and contractors, the net cost to the City in paying the 101 Ash Purchase Price could be substantially reduced.

#### **4. Public Purposes and Benefits of Implementing the Settlement Agreement**

The City's actions to resolve the pending disputes with Cisterra and Lender and to acquire fee title ownership of the Properties, including the payment of funds under the Agreement, will achieve numerous public purposes and benefits to the City, including, but not limited to:

- The City will obtain long-term control and ownership of the Properties, and the restrictive provisions of the existing lease-to-own agreements will terminate and no longer apply to the Properties. As the fee title owner of the Properties, the City will be able to use and operate the Properties as it deems appropriate and to explore a wide range of options with respect to the Properties, which could include, for example: (a) retention and renovation of the existing buildings, and occupancy of the buildings for public purposes, such as administrative office space for City employees; (b) demolition of the existing buildings and redevelopment of the Properties for public purposes; or (c) use of the Properties as part of a larger assemblage of City-owned downtown properties for a future mixed-use redevelopment project.
- In the Agreement, the Settling Parties will completely resolve the pending litigation between them and release all past and pending claims between them pertaining to the Properties. Accordingly, the Agreement will both eliminate a contingent liability for the City in an amount that cannot be predicted at this time and avoid the need to further defend against claims asserted by Cisterra and Lender.
- The Agreement will eliminate the City's need to incur substantial costs to defend against the claims of Cisterra and Lender in the pending litigation and will further eliminate the risk that the City could be compelled to pay the attorneys' fees and costs of Cisterra and Lender in the event of an unsuccessful outcome in the litigation.

- The Agreement will provide monetary benefits to the City, in that: (a) the City will not be responsible for payment of any attorneys' fees and costs incurred to date by Cisterra and Lender; (b) Cisterra will relinquish 100 percent of its past profit on the Prior 101 Ash Transactions in the amount of \$7,452,500; and (c) Lender will waive any penalties for prepayment of the CCP Loan and the 101 Ash Loan, resulting in a cost savings in excess of \$11.7 million relative to what Lender is contractually permitted to recover under the CCP Loan and the 101 Ash Loan.
- The City will reserve the right to pursue pending and future legal claims for monetary recovery against Jason Hughes and related entities, as well as the insurance carriers for the 101 Ash Property and the contractors who performed the 101 Ash Renovations.